Fundamentals Level – Skills Module

Taxation (Pakistan)

Thursday 7 December 2017

Time allowed: 3 hours 15 minutes

This question paper is divided into two sections:

Section A – ALL 15 questions are compulsory and MUST be attempted

Section B – ALL SIX questions are compulsory and MUST be attempted

Tax rates and allowances are on pages 2–5.

Do NOT open this question paper until instructed by the supervisor.

Do NOT record any of your answers on the question paper.
This question paper must not be removed from the examination hall.

Paper F6 (PKN)

Think Ahead ACCA

The Association of Chartered Certified Accountants

SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest rupee.
2. All apportionments should be made to the nearest month except where the exact number of days is given in the question.
3. All workings should be shown in Section B.

TAX RATES AND ALLOWANCES

The following tax rates and allowances for the tax year 2017 are to be used in answering the questions.

A. Tax rates for salaried individuals – where salary income exceeds 50% of taxable income

Taxable income	Rate of tax on taxable income
0 to Rs. 400,000	0%
Rs. 400,001 to Rs. 500,000	2% of the amount exceeding Rs. 400,000
Rs. 500,001 to Rs. 750,000	Rs. 2,000 plus 5% of the amount exceeding Rs. 500,000
Rs. 750,001 to Rs. 1,400,000	Rs. 14,500 plus 10% of the amount exceeding Rs.750,000
Rs. 1,400,001 to Rs. 1,500,000	Rs. 79,500 plus 12·5% of the amount exceeding Rs. 1,400,000
Rs. 1,500,001 to Rs. 1,800,000	Rs. 92,000 plus 15% of the amount exceeding Rs. 1,500,000
Rs. 1,800,001 to Rs. 2,500,000	Rs. 137,000 plus 17·5% of the amount exceeding Rs. 1,800,000
Rs. 2,500,001 to Rs. 3,000,000	Rs. 259,500 plus 20% of the amount exceeding Rs. 2,500,000
Rs. 3,000,001 to Rs. 3,500,000	Rs. 359,500 plus 22·5% of the amount exceeding Rs. 3,000,000
Rs. 3,500,001 to Rs. 4,000,000	Rs. 472,000 plus 25% of the amount exceeding Rs. 3,500,000
Rs. 4,000,001 to Rs. 7,000,000	Rs. 597,000 plus 27·5% of the amount exceeding Rs. 4,000,000
Rs. 7,000,001 and above	Rs. 1,422,000 plus 30% of the amount exceeding Rs. 7,000,000

B. Tax rates for associations of persons and non-salaried individuals to whom the rates given in A are not applicable [Not being income from house property]

Taxable income	Rate of tax on taxable income
0 to Rs. 400,000	0%
Rs. 400,001 to Rs. 500,000	7% of the amount exceeding Rs. 400,000
Rs. 500,001 to Rs. 750,000	Rs. 7,000 plus 10% of the amount exceeding Rs. 500,000
Rs. 750,001 to Rs. 1,500,000	Rs. 32,000 plus 15% of the amount exceeding Rs. 750,000
Rs. 1,500,001 to Rs. 2,500,000	Rs. 144,500 plus 20% of the amount exceeding Rs. 1,500,000
Rs. 2,500,001 to Rs. 4,000,000	Rs. 344,500 plus 25% of the amount exceeding Rs. 2,500,000
Rs. 4,000,001 to Rs. 6,000,000	Rs. 719,500 plus 30% of the amount exceeding Rs. 4,000,000
Rs. 6,000,001 and above	Rs. 1,319,500 plus 35% * of the amount exceeding Rs. 6,000,000.

* in the case of a professional firm which by law is prohibited from incorporation, the rate will be 32%.

C Tax rates for individuals and association of persons in respect of income from house property

Where the gross amount of rent	
– does not exceed Rs. 200,000	Nil
– exceeds Rs. 200,000 but does not exceed Rs. 600,000	5% of the amount exceeding Rs. 200,000
– exceeds Rs. 600,000 but does not exceed Rs. 1,000,000	Rs. 20,000 plus 10% of the amount exceeding Rs. 600,000
– exceeds Rs. 1,000,000 but does not exceed Rs. 2,000,000	Rs. 60,000 plus 15% of the amount exceeding Rs. 1,000,000
– exceeds Rs. 2,000,000	Rs. 210,000 plus 20% of the amount exceeding Rs. 2,000,000

D. Corporate tax rates for companies

Small company	25% of taxable income
Public company/private company	31% of taxable income
Tax rate for foreign direct investment in industrial undertakings by companies	20% of taxable income

E. Alternative corporate tax rate for companies	17% of accounting income
F. Super tax for companies other than banks	3% of income

G. Tax rates on capital gains on the disposal of securities

	Filer	Non-filer
Where the holding period of a security		
– is less than one year	15%	18%
– is one year or more but less than two years	12·5%	16%
– is two years or more but the security was acquired on or after 1 July 2012	7·5%	11%
– was acquired before 1 July 2012	0%	0%

H. Tax rates on capital gains on the disposal of immovable properties

(i) Where an immovable property was acquired on or after 1 July 2016 and its holding period is	
– up to one year	10%
– more than one year but not more than two years	7·5%
– more than two years but less than three years	5%
– more than three years	0%
(ii) Where an immovable property was acquired before 1 July 2016 and its holding period is	
– up to three years	5%
– more than three years	0%

I. Rate for profit on debt

Where profit on debt does not exceed Rs 25,000,000	10%
Where profit on debt exceeds Rs 25,000,000 but does not exceed Rs 50,000,000	Rs. 2,500,000 plus 12·5% of the amount exceeding Rs 25,000,000
Where profit on debt exceeds Rs 50,000,000	Rs 5,625,000 plus 15% of the amount exceeding Rs 50,000,000

J. Rates of deduction/collection of tax at source

Sale of goods (general rate)		
– where the payment is being made to a company being a	– filer	4%
	– non-filer	6%
– where the payment is being made to a taxpayer other than a company being a	– filer	4·5%
	– non-filer	6·5%
Sale of immovable property by a	– filer	1%
	– non-filer	2%
Purchase of immovable property having a value of more than Rs. 4 million by a	– filer	2%
	– non-filer	4%

Services (other than transport and media)		
– where the payment is being made to a company being a		
	– filer	8%
	– non-filer	12%
– where the payment is being made to a taxpayer other than a company being a		
	– filer	10%
	– non-filer	15%
On payment made to an electronic or print media for advertising services being a filer		1·5%
On payment made to an electronic or print media for advertising services being a non–filer		
	– company	12%
	– other than a company	15%
Contracts other than a contract by a sports person		
– where the payment is being made to a company being a		
	– filer	7%
	– non-filer	10%
– where the payment is being made to a taxpayer other than a company being a		
	– filer	7·5%
	– non-filer	10%
Contract by a sports person		10%
Commission and brokerage received by a non-filer		15%
Commission and brokerage received by a filer being		
– an advertising agent		10%
– other than an advertising agent		12%
Profit on debt received by a		
– filer		10%
– non-filer where the amount of profit does not exceed Rs. 500,000		10%
– non-filer where the amount of profit exceeds Rs. 500,000		17·5%
Import of goods (general rate)		
– in the case of industrial undertakings being a		
	– filer	5·5%
	– non-filer	8%
– in all other cases of companies being a		
	– filer	5·5%
	– non-filer	8%
– in the case of other taxpayers being a		
	– filer	6%
	– non-filer	9%
On domestic electricity bills of Rs. 75,000 or more per month		7·5% of the bill
On an international air-ticket of		
– first or executive class		Rs. 16,000 per person
– others excluding economy class		Rs. 12,000 per person
– economy class		Rs. 0
On the fee received by a director of a company for attending a meeting etc		20%
General rate on the dividends received from a company by a		
	– filer	12·5%
	– non-filer	17·5%

K. Depreciation rates

Buildings (all types)	10%	of the tax written down value
Furniture and fittings	15%	
Plant and machinery (not otherwise specified)	15%	
Motor vehicles (all types)	15%	
Computer hardware	30%	

L. Initial allowance on eligible assets

Buildings	15%	of cost
Plant and machinery	25%	

M. Pre-commencement expenditure

Amortisation rate for pre-commencement expenditure	20%

N. Benchmark rate

Interest free loans to employees	10% per annum

Section B – ALL SIX questions are compulsory and MUST be attempted

Please write your answers to all parts of these questions on the lined pages within the Candidate Answer Booklet.

1 (a) **Explain the difference between the cash-basis of accounting and the accrual-basis of accounting.** (2 marks)

(b) **State the procedure for changing the method of accounting used for computing income from business and the adjustments which will need to be made in the computation of income on adopting such a change.** (4 marks)

(c) For the tax year 2017, Abid declared the following incomes/losses:

	Rs.
Salary	3,450,000
'Income from other sources' assessable under the normal tax regime	550,000
Loss under the head 'speculation business'	(500,000)
'Income from business' assessable under the normal tax regime	1,000,000
Brought forward loss under the head 'income from business' assessable under the normal tax regime from the tax year 2016	(1,500,000)

Required:

Compute the tax liability of Abid for the tax year 2017. Give reasons for the treatment of each of the loss items. (4 marks)

(10 marks)

2 Durrani Chemicals Ltd (DCL) was incorporated under the Companies Ordinance, 1984 on 20 June 2015 with a paid up capital of Rs. 6,000,000 which was raised through the issuance of shares for cash. DCL set up a pesticide manufacturing unit on 1 December 2015 at a total cost of Rs. 7,000,000 which was financed by equity of Rs. 6,000,000 and a loan from a commercial bank of Rs. 1,000,000. The unit started commercial production on 1 July 2016. DCL is eligible for a tax credit on account of its newly established industrial undertaking of pesticide manufacturing under s.65D of the Income Tax Ordinance, 2001. The taxable income of DCL for the tax year 2017 was Rs. 1,200,000. DCL is not a small company.

Required:

(a) **State, with reasons, the initial and terminal dates during which the taxable income of Durrani Chemicals Ltd will be given a tax credit on account of its newly established pesticide manufacturing unit.** (2 marks)

(b) **Compute the tax credit available to Durrani Chemicals Ltd for the tax year 2017.** (3 marks)

(c) (i) **State the situations under which the tax credit availed to Durrani Chemicals Ltd may subsequently be treated as having been wrongly allowed by the Commissioner.** (2 marks)

(ii) **State the consequences for Durrani Chemicals Ltd if the tax credit availed of is subsequently treated as being wrongly allowed.** (3 marks)

(10 marks)

3 For this question you should assume that today's date is 15 July 2017.

Intisar, a resident of Pakistan, disposed of the following assets during the year ended 30 June 2017:

(1) 1 December 2016: Sold an antique coin for Rs. 100,000. The coin had been purchased for Rs. 125,000 on 1 July 2016. The transactional cost incurred was Rs. 2,000.

(2) 15 December 2016: Sold unimproved land for Rs. 1,765,000. The land had been acquired for Rs. 1,365,000 on 10 January 2016 and in addition capital value tax of Rs. 35,000 was paid in cash to the government. The land was used by Intisar for his business in the tax year 2016 but no business was conducted there during the tax year 2017.

(3) 31 December 2016: Sold his guest house to Company Wye Ltd for Rs. 10,000,000. The guest house had been purchased for Rs. 7,000,000 on 1 July 2016. Intisar incurred Rs. 50,000 on minor repairs and Rs. 500,000 on the major renovation of the guest house. The registration authority collected income tax of Rs. 200,000 from Intisar at the time of the transfer of the guest house.

(4) 15 January 2017: Sold commercial papers issued by the Government of the Punjab for Rs. 1,240,000 which Intisar had purchased on 20 April 2016 for Rs. 1,110,000.

(5) 31 March 2017: Sold an antique saloon car for Rs. 2,500,000. The car had been acquired for Rs. 1,500,000 on 1 April 2010. Brokerage commission of Rs. 8,000 was paid to a car dealer on acquisition.

Other information

(i) Intisar has a brought forward loss of Rs. 350,000 on the disposal of shares in a listed company in the tax year 2016.

(ii) Motor vehicle tax paid by Intisar on 30 June 2017 was Rs. 18,000.

Required:

Compute the total tax payable by Intisar on the taxable income arising from the above transactions on the filing of his tax return for the tax year 2017. Give brief reasons for your treatment of each item.

Note: The reasons/explanations for the items not listed in the computation should be shown separately, as specific marks are allocated for these explanations.

(10 marks)

4 For this question, you should assume that today's date is 1 March 2017.

Badar is a registered person under the Sales Tax Act, 1990, and is engaged in the business of the manufacture and supply of goods chargeable to sales tax at the standard rate of 17%. His business transactions for the month of February 2017 were as follows:

(1) Sales including exports, exclusive of sales tax:

		Rs.
(i)	Local supplies to unregistered persons	4,000,000
(ii)	Local supplies to registered persons	5,000,000
(iii)	Local supplies to diplomats in Islamabad covered under the Fifth Schedule	1,000,000
(iv)	Exports to Dubai with the intention of re-importing the same to Pakistan by a registered person	3,000,000

(2) Payments for raw material purchases, inclusive of sales tax, made to the following registered persons:

		Rs.
(i)	To Manahil in cash	46,800
(ii)	To Zahid through a crossed cheque drawn on a personal bank account of Badar fully verifiable	3,510,000
(iii)	To Nazir through an online payment from the business account of Badar to the business account of Nazir, verifiable from the bank statements of Badar and Nazir	8,190,000

(3) An electricity bill of Rs. 600,000 paid in cash which included a sales tax amount of Rs. 114,000.

(4) An amount of Rs. 1,053,000 inclusive of sales tax due to Ilyas a supplier of raw materials, was outstanding for 181 days on 1 February, 2017. Badar has already claimed the amount of input tax as per the sales tax invoice issued by Ilyas.

Required:

(a) Explain what is meant by a 'business bank account' under the Sales Tax Act, 1990. (2 marks)

(b) Compute the sales tax payable by Badar with his sales tax return for the month of February 2017. (8 marks)

(10 marks)

5 For this question, you should assume that today's date is 15 July 2017.

Plastic Goods (Pvt) Limited (PGPL) is a company incorporated under the Companies Ordinance, 1984. The control and management of the affairs of PGPL was situated partly outside Pakistan during the year ended 30 June 2017. PGPL is not a small company. The products of PGPL are exempt from sales tax.

PGPL's income statement for the year ended 30 June 2017 is as follows:

	Note	Rs.	Rs.
Sales			140,000,000
Cost of sales	(1)		(100,000,000)
Gross profit			40,000,000
Administrative expenses	(2)	7,000,000	
Selling and distribution expenses	(3)	6,250,000	
Legal and financial charges	(4)	3,000,000	
Irrecoverable trade receivables	(5)	750,000	
			(17,000,000)
			23,000,000
Other income	(6)		1,500,000
Profit before tax			24,500,000
Provision for taxation			(7,595,000)
Net profit			16,905,000

All the expenditure has been made through crossed cheques drawn on a scheduled bank and tax has been duly deducted unless stated otherwise.

Notes

Note 1

Cost of sales includes:

(i) Amortisation of the cost of development of a new manufacturing process of Rs. 2,000,000. The development cost was capitalised as an intangible asset in 2005. The intangible has a useful life of 15 years.

(ii) Accounting depreciation of Rs. 2,500,000.

Note 2

Administrative expenses include:

(i) 1% of sales transferred to a reserve maintained for the welfare of PGPL's staff.

(ii) Entertainment expenditure of Rs. 400,000 incurred during the year at the time a new sales outlet of PGPL was opened. [s.20(1) and rule 10(1)(e) of the IT Rules, 2002]

(iii) Salary of Rs. 750,000, paid in cash, during the year to a temporary worker.

Note 3

Selling and distribution expenses include a car valued at Rs. 1,700,000 given to Mr Shahid, a dealer, for making a record high level of sales of PGPL's products in the six months ended on 31 December 2016. Mr Shahid is a filer, therefore no tax was collected from him.

Note 4

Legal and financial charges include:

(i) Rs. 350,000 paid as lease rentals for a truck to an approved leasing company (see note 7) consisting of a mark up of Rs. 50,000 and a principal amount of Rs. 300,000.

(ii) Legal fees of Rs. 900,000 in connection with an increase in PGPL's share capital.

Note 5

Irrecoverable receivables include a provision of Rs. 700,000 made on the principle of prudence because based on the experience of past years, it is estimated that 0·5% of sales result in bad debts.

Note 6

Other income of Rs. 1,500,000 represents the appreciation in the value of an investment held by PGPL in the form of shares in an associated company.

Note 7

PGPL's fixed asset records show the following:

Asset	Tax written down value (TWDV) as at 1 July 2016	Additions in the year	Total
	Rs.	Rs.	Rs.
Building on freehold land	4,000,000	–	4,000,000
Plant and machinery	7,000,000	–	7,000,000
Trucks	1,000,000	3,700,000 (sub-note a)	4,700,000
Computer hardware	560,000	140,000	700,000
Furniture and fixtures	800,000	100,000	900,000

Sub-note (a)

This amount represents all the lease rentals which PGPL will have to pay to the approved leasing company over the entire lease term of the truck, including the residual value under the finance lease agreement (see note 4(i)).

Note 8

PGPL has paid the following amounts of tax during the tax year 2017:

	Rs.
Total advance tax in four equal instalments	7,000,000
Tax collected along with electricity bills	400,000
Tax collected by the leasing company at the time of the lease because PGPL was mistakenly treated as a non-filer	111,000

Required:

(a) State, with reasons, whether during the tax year 2017 Plastic Goods (Pvt) Limited was or was not a resident in Pakistan. (2 marks)

(b) Compute the taxable income of Plastic Goods (Pvt) Limited for the tax year 2017 under the appropriate heads of income, giving clear reasons/explanations for the inclusion in or exclusion from the computation of each of the items listed in the question.

Note: The reasons/explanations for the items not included in the computation of taxable income should be shown separately as specific marks are allocated for this part of the requirement. (11 marks)

(c) Calculate the tax payable by/refundable to Plastic Goods (Pvt) Limited for the tax year 2017.

Note: Ignore the workers welfare fund, minimum tax and the alternative corporate tax provisions. (2 marks)

(15 marks)

6 For this question, you should assume that today's date is 15 July 2017.

Ejaz, aged 55, is employed as a salesman by Farwa Pharmaceuticals (Pvt) Ltd (FPPL). His earnings and relevant expenditures for the tax year ended 30 June 2017 are as follows:

Current employment:

(1) A basic salary of Rs. 25,000 per month.

(2) A utility allowance at 5% of his basic salary. This payment is gratuitous and not covered in his employment agreement.

(3) Commission earnings for the year of Rs. 375,000.

(4) Training allowance of Rs. 10,000 per month for the training of newly recruited trainee salesmen.

(5) In February 2017, Ejaz won the salesman of the year award. The award consisted of paid holiday of 15 days along with tickets and a hotel stay in Bali, Indonesia, at a total cost of Rs. 450,000.

(6) Ejaz is provided with a car by FPPL which cost the company Rs. 1,150,000. The running expenses of the car incurred during the year and reimbursed fully by FPPL were Rs. 230,000. The log book of the car showed personal use of the car as 20%.

(7) In addition to a medical allowance at 9% of his basic salary, Ejaz was also reimbursed treatment expenses of Rs. 430,000 for indoor treatment at a private hospital, in accordance with the terms of his employment.

(8) Ejaz and FPPL each contribute Rs. 2,500 per month towards a recognised provident fund.

(9) FPPL advanced Ejaz a loan of Rs. 1,000,000 on 1 January 2016 at a mark up of 2% per annum as per the policy of the company.

(10) Ejaz opted for an employee share scheme under which he was issued 5,000 shares in Marwa Pharmaceuticals (Pvt) Ltd, an associated company of FPPL, for Rs. 400,000 on 1 March 2015. These shares could only be sold on or after 1 April 2017. However, Ejaz sold the shares on 1 July 2017 for Rs. 900,000. The fair market value of the shares on relevant dates was as follows:

	Rs.
1 March 2015	500,000
1 April 2017	800,000
30 June 2017	890,000
1 July 2017	900,000

(11) Ejaz had to spend one week in a risky area in connection with a sales campaign for a new product for which he was given a dangerous working condition supplement of Rs. 50,000.

(12) Other receipts

A labour court awarded Ejaz Rs. 900,000 in respect of his unfair dismissal claim against his former employer. When making payment of the awarded amount, his former employer withheld tax of Rs. 90,000. Ejaz paid Rs. 80,000 to his lawyer through a crossed cheque in connection with the court proceedings leading to this award.

(13) Other amounts of tax withheld at source were:

(i) Rs. 190,000 by FPPL.
(ii) Rs. 3,000 along with telephone bills.
(iii) Rs. 8,000 in connection with a function held in a restaurant.

Required:

Compute Ejaz's taxable income and tax payable for the tax year 2017. Give reasons for the treatment of any items excluded from the taxable income or for which no expense/deduction is allowed.

(15 marks)

End of Question Paper